1991 Liberalisation and it's impact on India's growth

HS21205 : Macroeconomics

ARYAN GUPTA
20HS20011

Indian Institute of Technollogy Kharagpur

HS205 : Macroeconomics

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ARYAN GUPTA (20HS20011)

Relevance of Study

Liberalisation of 1991 Of India is the major turning point int the history of India. It changes the whole course of economic growth of India. Through this report we will understand how liberalization has influenced the economy of India in past 30 years. This reports is also helpful for developing country who are facing the same situation as was India in 1991 to know the significance of Liberalisation as a solution

Objective of Study

The objective of this study is to know the causes and policies of Liberalisation of India 1991. And also, to know the influence of Liberalization on India Economy in the past 30 years.

Introduction

Since independence, India has followed economic policies which aim to regulate and control the economy which was important in the early stage of independent India's journey. Some scholars argue that over the years these policies ended up hampering the process of growth and development of India while others think that these help India to start its developmental growth from near stagnation and help achieve growth in savings, industrial sector, and expansion in agriculture output. In 1991, India met with an economic crisis relating to its external debt in which the government was not able to make repayments on its borrowings from abroad and foreign exchange reserves. All these led the government to introduce a new set of economic policy measures in 1991 which changed the direction of our developmental strategies. In this economic reform of 1991, structural reforms can be seen with respect to liberalization, privatization and globalization.

Economic Crises of 1991

Indian Economic Reform of 1991 was the result of its economic crisis of 1991 which was resulted from poor economic policies, political instability, inefficient public sectors units, and resulting trade deficits leading to a balance of payment. Overvaluation of currency and the deficit of current accounts were also a factor responsible for the cause of crises. During this time there was a sharp depreciation of the exchange rate.

The economic crisis was primarily due to the large and growing fiscal imbalances over the 1980s. India's economic problem started worsening during the mid-eighties when it started to have balance of payments problems. Because of the Gulf War, India's oil import bill raised, exports slumped, credit dried up, and investors took their money out. Large fiscal deficits, over time, caused a spillover effect on the trade deficit resulting in culmination in an external payments crisis. Further, the collapse of the USSR Bloc, with which India had rupee exchange in trade, also worsened the situation. By the end of the 1980s, India was in serious economic trouble.

The gross fiscal deficit of the government (both center and states) rose from 9.0 % of Gross Domestic Product (GDP) in 1980-81 to 10.4 % in 1985-86 and to 12.7 % in 1990-91. For the center alone, the gross fiscal deficit rose from 6.1 % of GDP in 1980-81 to 8.3 % in 1985-86 and to 8.4 % in 1990-91. Since these deficits had to be met by borrowings, the internal debt of the government accumulated rapidly, rising from 35 % of GDP at the end of 1980-81 to 53 % of GDP at the end of 1990-91. During crises, the foreign exchange reserves had dried up to the point that India could barely finance three weeks' worth of imports.

Foreign Exchange Reserves in Selected Countries

(USD billion)

	1990	1991	1992	1993	1994	1995	1996
India	1.21	3.58	5.46	9.81	19.39	17.47	197.42
China	28.59	42.66	19.44	21.20	51.62	73.58	98.85
Indonesia	7.35	9.15	10.18	10.99	11.82	13.31	15.06
Malaysia	9.33	10.42	16.78	26.81	24.89	22.95	25.21

Recovery from Crises

With India's foreign exchange reserves at $1.2 billion in January 1991 and depleted by half by June, barely enough to last for roughly 3 weeks of essential imports, India was only weeks away from defaulting on its external balance of payment obligations.

The government of India's immediate response was to secure an emergency loan of $2.2 billion from the International Monetary

Fund by pledging 67 tons of India's gold reserves as collateral security, jolting the country out of an economic slumber. The then Chandra Shekhar government had collapsed a few months after pledging the country's entire gold reserves against the loan. The move helped tide over the balance of payment crisis and kick-started P. V. Narasimha Rao's economic reform process.
After P.V Narasimha Rao took over as Prime Minister and Manmohan Singh as Finance minister many economic reforms took place which was termed as Economic Reform of 1991. It contains liberalization, privatization, and globalization policy. Reforms start with the devaluation of Indian rupees.

Liberalisation of 1991

It refers to the economic liberalization of various economic policies to loosen government control by expanding the role of private and foreign investment. Before 1991, also attempts were made to liberalize the economy but they were unsuccessful. Before it, rules and laws which were aimed at regulating economic activities became major hindrances in growth and development. Liberalisation was introduced to put an end to these restrictions and open various sectors of the economy. Though a few liberalization measures were introduced in the 1980s in areas of industrial licensing, export-import policy, technology upgradation, fiscal policy, and foreign investment, reform policies initiated in 1991 were more comprehensive.

Liberalisation Policies

- **Deregulation of Industrial Reform**

Before liberalisation, regulatory mechanisms were enforced in various ways. Under industrial license raj the government control was so strong that permission is required by government officials to start a firm, close a firm or decide the amount of goods that could be produced. The private sector was not allowed in many fields and some goods can only be produced in small scale industries. The government has also control over price fixation and distribution of a selected industrial product.

The reform policies of 1991 removed many of these restrictions. Now, industrial licensing was abolished for almost all products except alcohol, cigarettes, hazardous chemicals, industrial explosives, electronics, aerospace and drugs, and pharmaceuticals. The only industries which are now reserved for the public sector are a part of atomic energy generation and some core activities in railway transport. Many goods produced by small-scale industries have now been dereserved. Now the market has been allowed to determine the prices in most industries.

- **Financial Sector reforms**

The important reform made in the exchange market was in the foreign exchange market. The rupees were devalued against other foreign currencies and rupee value determination was set free from governmental control to resolve the immediate balance of payments issue. Now market started determining the exchange rate according to the demand and supply of foreign exchange.

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- **Trade and Investment policy reforms**

During initial independence, to protect its domestic industries from foreign competition, India started following quantitative restriction on imports which means tight control was put over imports, and tariffs was also kept very high. These policies reduced efficiency and competitiveness which led to slow growth of the manufacturing sector.

So, liberalisation of trade and investment was done by keeping the aim of improving the international competitiveness of industrial production and also to increase foreign investment and adoption of modern technologies into the country. Steps taken in trade policy reforms were removing quantitative restrictions on imports and exports, reduction of tariff rates, and removal of licensing procedures for imports except in the case of hazardous and environment sensitive industries.

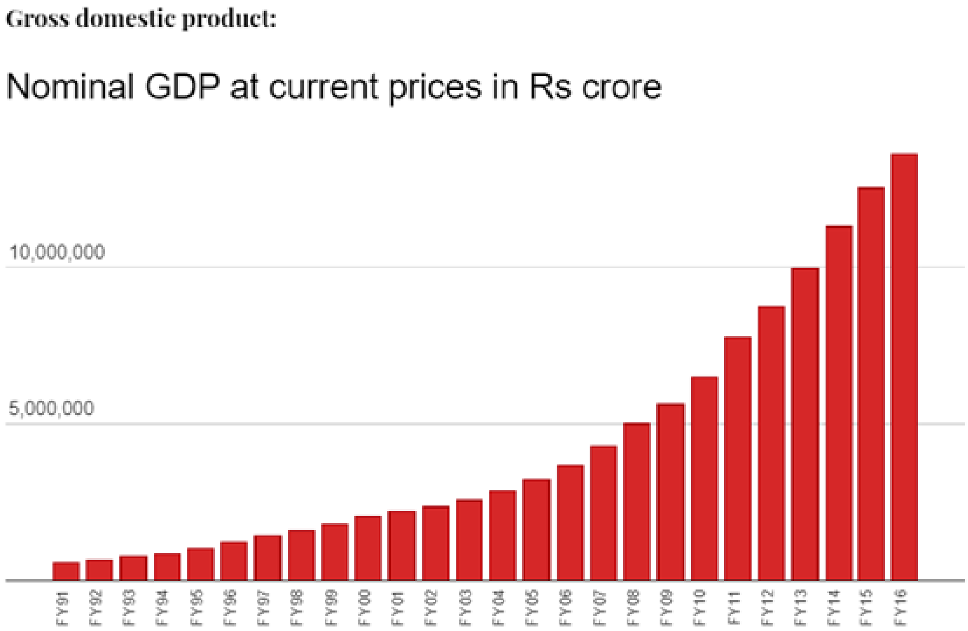
- **Tax reforms**

Since reforms of 1991, there has been a constant reduction of taxes on individual income as it is believed high tax rates were responsible for tax evasion. The earlier very high corporation tax has been gradually reduced. The policies on Indirect taxes on different comedies are also reformed to establish a common national market for goods and comedies.

Impact of 1991 Liberalisation

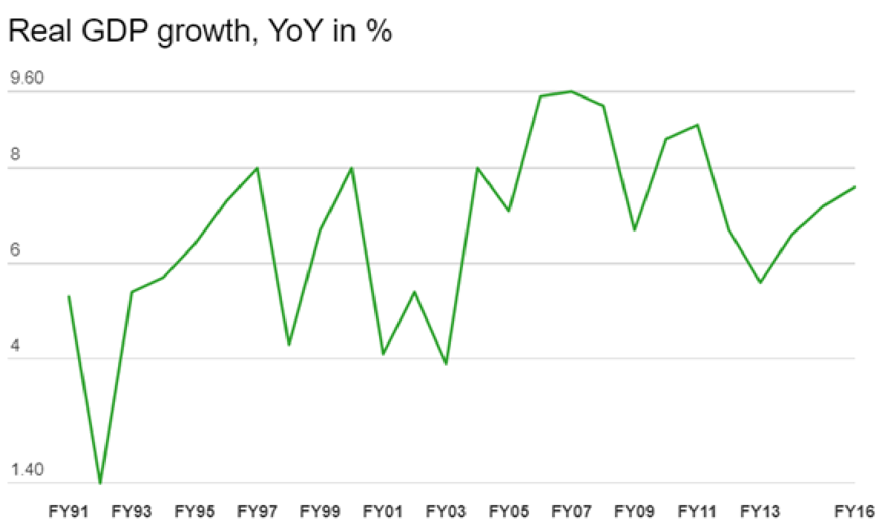
Some of the changes on economic factors of country after the 1991 liberalisation.

GDP is an important measure of a country that how well the country is economically doing and how big the economy is. India's GDP stood Rs. 5,86,212. Since liberalization India's GDP rise rapidly. About 25 years later, it stands at Rs 1,35,76,086 crore, up 2216 percent. In dollar terms, India's GDP crossed the $2 trillion mark in 2015-16.



- **Real GDP Growth**

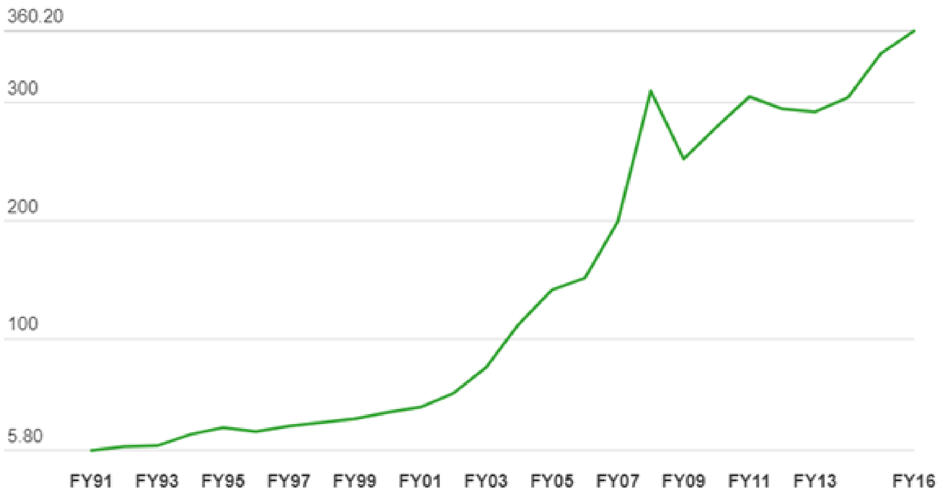
.Before reforms, once admonished for its low economic growth, India remained the second fastest growing economy in the world, behind China until 2015. Especially, between 2005 and 2008, the economy clocked the 9% mark annually. In 2015-16 India was the fastest growing economy in the world with a growth rate of 7.6%.



- **Foreign Direct Investment**

Before 1991, foreign investment was negligible. However, investments have steadily risen since then, except for occasional blips between 1997 and 2000 and 2008 and 2012 – owing to the global economic slowdown. The year 2008 recorded the highest FDI inflow of $43.40 billion. The biggest spurt in inflow was between 2005 and 2006 – 175.54%. In 2015, India received $63 billion and replaced China as the top FDI destination, according to The Financial Times.

Foreign exchange reserves in $billion (cumulative)



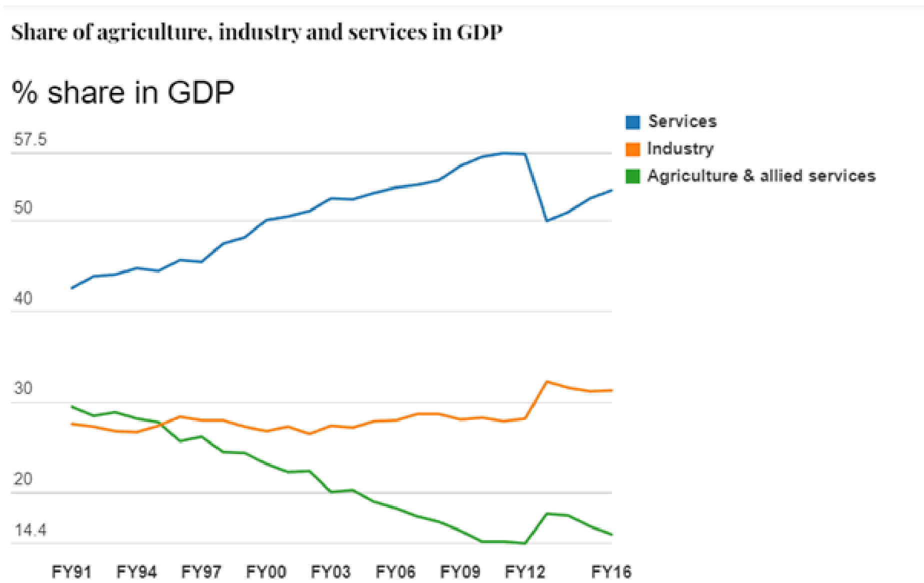
Source: RBI Get the data

- **Purchasing Power Parity**

.Purchasing power parity (PPP) gives a comprehensive idea of the standard of living and the cost of living in a particular country. Since 1991, the standard of living has improved for sure. However, the cost of living has risen too. In 1991, per capita PPP was $1,173. In 2014, it rose nearly five-fold to $5,701.

- **Share of agriculture, industry and service in GDP**

After the reform of 1991, there is a gradual decrease in the contribution of the agriculture sector to India's economy. India's traditional occupation, agriculture now contributes only about 15% to the GDP, down from 29 percent in 1991. Now service sector has emerged as the highest contributor to the national economy. The industrial sector has also undergone marginal growth in the last 30 years



Conclusion

There have been many revolutionary changes in the economy of India since 1991 and has a great impact on all the areas of life in it. The relaxation of government regulation in the country allows .

the private sector to operate the business more freely. The opening of the economic border to multinationals and foreign investments allows the improved inflow of capital in the country. Stock market prices also went up. Investors get benefits by being able to invest a portion of their portfolio into a diversifying asset class. Liberalisation also has a huge positive impact on other things like agriculture where cropping pattern has undergone a huge modification.

Despite the many positive impacts of liberalisation, it also has some negative effects. After liberalization competition increased for local and small firms as multinational companies started coming to India. Economy .Due to tremendous change Indian economy remain destabilized. Government stake in bank and insurance decreases due to increase of foreign direct investment in them. Rapid change in technology forces small firms to either adapt or close their business.

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